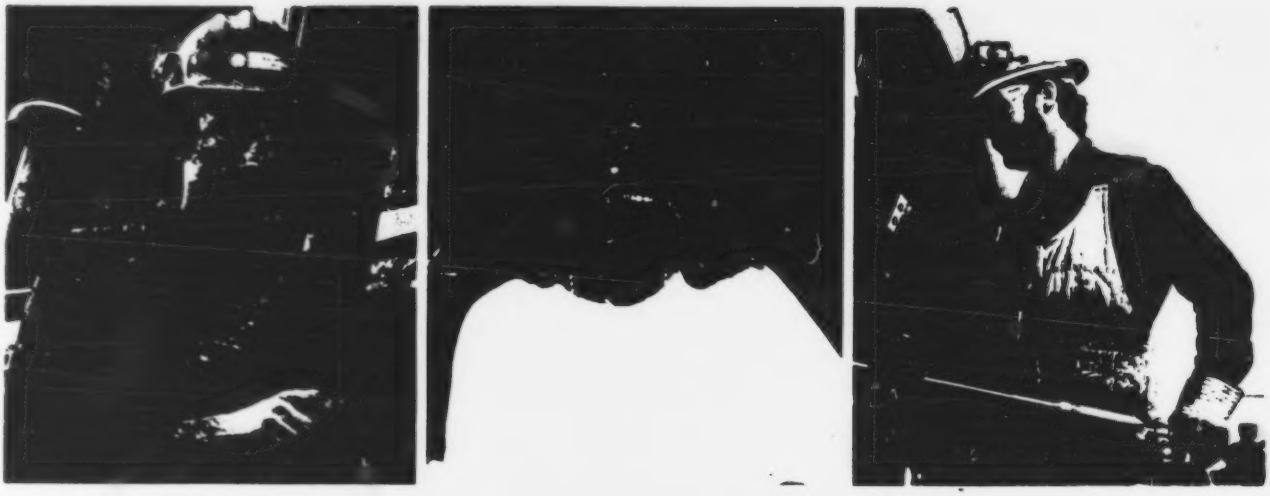
THE BRITISH COLUMBIA RAILWAY GROUP OF COMPANIES

ANNUAL REPORT FOR 1985

CORPORATE STATEMENT



BC Rail employs 2,620 people between North Vancouver and the railway's northern terminus in Fort Nelson, B.C.

The British Columbia Railway group comprises three companies:

- ☐ British Columbia Railway Company, which holds investments in its two subsidiary companies —
- ☐ BCR Properties Ltd., which owns and manages the group's non-operating real estate assets and
- ☐ BC Rail Ltd., which is the group's railway operating company.

The Province of British Columbia is the sole shareholder of British Columbia Railway Company, which holds 100 per cent of the common shares of BCR Properties Ltd. BCR Properties owns 75 per cent of the common shares of BC Rail Ltd., the remaining 25 per cent of which are held by British Columbia Railway Company.

In 1984, BC Rail Ltd. offered eight million Series 'A' Preferred Shares for sale on Canadian stock exchanges, at a unit price of $25. The non-voting stock offer was fully-subscribed and the capital raised was used to acquire operating railway assets from British Columbia Railway Company which in turn, retired short-term borrowings.

The railway's principal sources of revenue are the transportation of forest industry-related products and coal from British Columbia's northeastern coalfields. All told, BC Rail operates and maintains 1,390 miles of main track between North Vancouver and its northernmost terminal in Fort Nelson, B.C.

BC Rail has online connections to all rail-served points in North America. Group assets exceed $1.2 billion.

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Woodchip transportation is an important source of revenue.

BOARD OF DIRECTORS

J. Norman Hyland, *Chairman*
S. C. Cooper
Hon. Jack Heinrich*
Stanley M. Horner
E. Cecil Hurd
John C. Kerr**
E. A. Moffat
M. C. Norris
Bruce Rome

* *Mr. Heinrich joined the Board in April, 1985. He succeeded Hon. Don M. Phillips, who retired from the Board in March.*

***Mr. Kerr resigned from the Board early in 1986. The position is temporarily vacant.*

OFFICERS

M. C. Norris *President and Chief Executive Officer*
J. R. Clarke *Vice-President - Finance*
Brian Foley *Vice-President - Industrial Relations*
N. A. McPherson *Vice-President - Operations and Maintenance**
G. L. Ritchie *Vice-President - Administration and Secretary*
A. C. Sturgeon *Vice-President - Marketing and Sales***

**Mr. McPherson retired from the company in December, 1985.*

***Mr. Sturgeon was appointed Senior Vice-President, responsible for Operations and Maintenance, as well as Marketing and Sales, in January, 1986.*

FINANCIAL HIGHLIGHTS

	(Dollars in Thousands) 1985	1984
Operating revenues	**$294,600**	$256,108
Operating expenses	**$216,239**	$189,199
Operating income	**$78,361**	$66,909
Net income before minority interest	**$61,430**	$42,687
Net income	**$42,930**	$34,342
Carloadings	**234,335**	200,257
Total tons hauled	**17,831,967**	14,672,412
Employees at year-end	**2,620**	2,640

DIRECTORS' REPORT

During 1985, the British Columbia Railway group benefited from an uninterrupted flow of product through its two principal freight revenue sources, namely the numerous forest product converting plants along its line and the two coal mines at Tumbler Ridge.

Unlike 1984, there were no industrial disputes to reduce the volume of pulp and lumber loadings and the shipments of coal came very close to the scheduled tonnage. As a result of this favourable operating environment, consolidated operating income increased to nearly $78.4 million, or 17 per cent greater than in 1984. Consolidated net income rose to nearly $43 million, an increase of 25 per cent over the preceding year.

This strong earnings result was matched by an equally strong cash generation, which after meeting interest payments and preferred dividend declarations, permitted a reduction in long term debt of approximately $48 million.

A reduction in debt is unlikely to be repeated in 1986, since a greater amount of the group's cash resources will be required for capital investment — principally for completion of the upgrading program on the mainline between Tacheeda and Prince George.

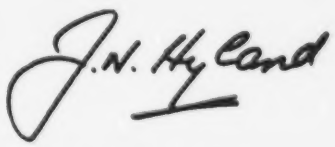
While 1983 and 1984 were years of expansion and capital restructuring for the company, 1985 was one of consolidation and emphasis on operating procedures and efficiencies. We anticipate that 1986 will continue this trend and if the industries which we serve maintain their current levels of production, the group should continue its favourable operating performance.

In March, 1985, the Hon. Don Phillips, MLA, retired from the Board. Mr. Phillips was appointed in 1975 and during his tenure was an enthusiastic and effective director. His counsel and experience contributed greatly to the company's growth and development.

The Hon. Jack Heinrich, MLA, was appointed to fill the vacancy created by Mr. Phillips's retirement. As a resident of Prince George, Mr. Heinrich is familiar with the operations of the group and its role of providing a reliable and efficient transportation service to and from the north and north-central interior of British Columbia.

In 1986, British Columbia and Vancouver will host a world exposition with the focus on transportation and communication. As major suppliers of both services, BC Rail will be an enthusiastic participant in several of the special programs planned for Expo '86.

The results of 1985 are testimony to the standard of the company's employees in every department and at all levels. To all of these, the Board extends its thanks and recognition for their contribution to a successful year.



J. N. Hyland, *Chairman*

PRESIDENT'S REPORT

I am pleased to report another excellent year for the group, which resulted in consolidated net income of $61.4 million, before dividend payments to preferred shareholders. This compares with net income of $42.7 million, before dividend payments, for the 1984 operating year.

The 1985 results mark our fourth consecutive year of record net income before payments of minority interest. The group's performance is tangible evidence that our continuing search for operational efficiency is bearing fruit and that increasingly, we are enjoying the benefits of more than a decade of capital investment and modernization.

Nineteen-eighty-five net income rose by 25 per cent, from $34.3 million in 1984 to $42.9 million in 1985, while revenues rose from $256.1 million to $294.6 million over the same period. The improved returns are partially due to an overall increase in carloadings and a continuing increase in northeastern coal shipments as the two producing mines neared or surpassed contracted tonnages.

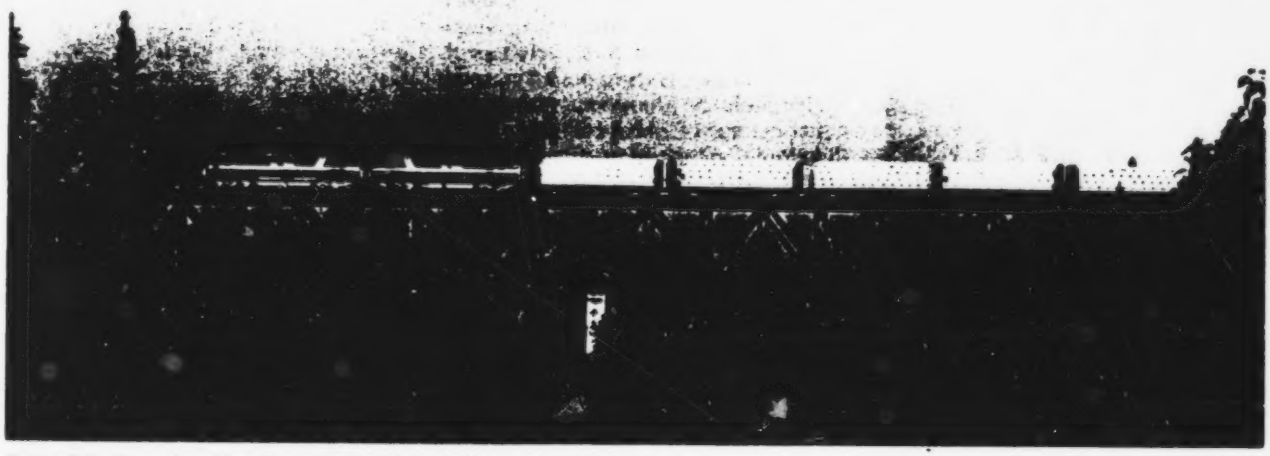
Rewarding as the results are, however, net income of $42.9 million reflects a return on assets of less than 3.5 per cent and a return on shareholder's equity of less than 5.5 per cent. North American railways are not normally considered to be "revenue adequate" unless return on investment exceeds 15.8 per cent and on that basis, it is evident we have a long way to go before our commercial returns can be considered adequate.

Carloadings are the lifeblood of our organization and for measuring the progress of a railway, there is no more effective yardstick. Last year, we loaded 234,335 cars of all kinds, compared with 200,257 the year before, an increase of 17 per cent. While this is encouraging, it is tempered by the knowledge that there will be few opportunities for significant traffic or revenue growth in the five years ahead.

BC Rail employees can take pride in their company's improving performance over the last few years but we cannot reasonably expect that the upward trend will continue forever. Rather, the earnings we generate in the good years must be reinvested to withstand downturns in the future.

In April last year, the railway became subject to provincial sales and fuel taxes, which will affect purchases of fuel and other materials in the years to come. The company paid approximately $6 million in fuel and sales taxes during the balance of the year. This additional liability, together with the prospect of very large increases in insurance premiums, will make it very difficult to improve the group's return on investment and assets in the immediate years ahead.

On a happier note, I am pleased to report that 1985 proved to be the company's best year ever for employee safety. The accident frequency rate is one downward trend I am always delighted to see and in 1985, the rate of accidents per million people-hours reached a record low of 27. The rate has been steadily declining since 1979, when it stood at 67 injuries per million people-hours.



Prime B.C. dimensional lumber southbound on Cottonwood bridge.

Operationally, the railway continued its efforts to improve safety and a great deal of the capital invested in track upgrading, grade and rock stabilization and bridge reconstruction was applied with safety foremost in mind. The work will continue through 1986 and approximately $388 million has been earmarked for capital improvements to physical plant during the next five years.

Concern for safety of train operations on the heavy-haul portion of the railway between Tacheeda and Prince George has precipitated further testing of both concrete and steel cross-ties under northern winter conditions. The nature of the traffic on this section of the line which involves 13,000 ton coal trains, as well as long regular freight trains, will require installation on curves of other than the traditional treated wooden ties used elsewhere in the system. The use of treated wooden cross-ties, however, will continue on most of the BC Rail system.

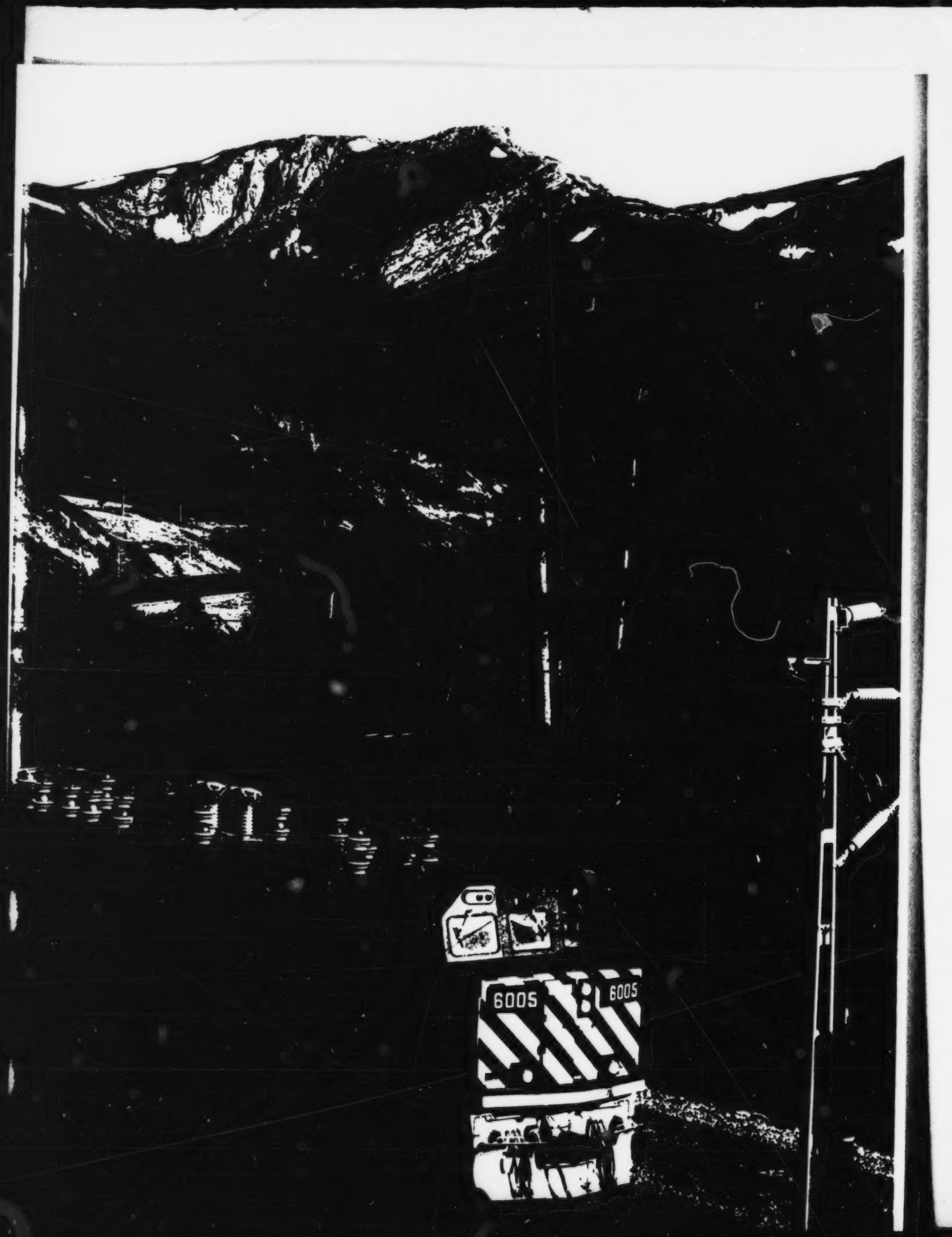
Together with my management committee colleagues and other railway employees, I was sorry to lose the services of our Vice-President — Operations and Maintenance, Mr. Norman McPherson, who retired for reasons of ill-health on December 13th. Mr. McPherson's knowledge and leadership will be sorely missed by us all.

In conclusion, I would like to acknowledge the continuing loyalty and efforts of all our employees, without which this fourth record year of operational and financial achievement would not have been possible. It was an exceptional year and thanks are due to highly competent BC Rail people throughout our system.

M.C. Norris

M.C. Norris, *President and Chief Executive Officer*

Right: A 98-car coal train on the 50kV electrified Tumbler Ridge line in northeastern British Columbia.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CARRIER
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THE YEAR IN REVIEW

Indonesia's Ombilin railway, where International Rail provided consulting expertise during 1985.

As well as continued and substantial improvement in the group's consolidated financial results, 1985 was marked by a number of interesting operational and regulatory developments.

Early in the year, BC Rail Ltd. and Swan Wooster Engineering Co. Ltd. announced the formation of International Rail Consultants, a joint venture created to offer consulting expertise to developing nations and elsewhere.

As the year progressed, the new group successfully tendered for consulting work in Kenya, Mozambique and Indonesia and towards year-end, engineering staff also visited The People's Republic of China.

The work in Africa was performed for the Southern African Transportation and Communications Commission and was funded by the Canadian International Development Agency. Activity is gaining momentum and the outlook for the new consulting arm is encouraging.

Later in January, the group's Real Estate and Industrial Development department was reorganized to become a profit centre under the new name Real Estate Development. Its mandate is to market development of the group's substantial land holdings and to intensify efforts to generate revenues from lands held by BCR Properties Ltd. and BC Rail.

The railway took delivery of five new SD-40 diesel-electric locomotives during the year, having earlier begun repainting its existing fleet of diesel locomotives and cabooses in the red, white and blue colour scheme, adopted in 1984 for electric units. To mark the world exposition being held in Vancouver from May to October this year, the new and repainted equipment will bear the official Expo '86 emblem. The BC Rail motive power fleet now consists of 110 diesel-electric locomotives; seven 6,000 h.p. all-electric units and six so-called 'slugs' — auxiliary electric units — used for yard duties.

Effective April 1st, 1985, the group began paying provincial fuel and sales taxes on all goods and services, an obligation from which the group thereto had been exempt. In the remaining nine months of the fiscal year, the company paid approximately $6 million in social services taxes and fuel taxes to the provincial government.

In recognition of the importance of forest products to the railway, a dedicated forest products unit was formed last spring. The objective was to improve communications between shippers and the railway

Left: Loading dimensional S.P.F. — spruce, pine and fir — in Prince George.

BC Rail's Cariboo Dayliner at the new Exeter station.

Grain elevators, Fort St. John.

and to meet transportation needs of the forest industry in the ever changing environment of competition and deregulation.

Some weeks later, however, the provincially-regulated BC Rail rates were themselves deregulated and with its new-found ability to deal individually with shippers, rather than having to adhere to published tariffs, the railway can now compete with American carriers on an equal footing.

During the year, the railway continued to upgrade its passenger car fleet. Major overhauls and refurbishing work were successfully carried out in the railway's own locomotive rebuild shops in Squamish, B.C. Near year-end, a ski-train between North Vancouver and the Whistler resort was introduced to accommodate increasing demand from both skiers and resort operators.

In other passenger service developments during the year, a new station was opened at Exeter, B.C., to replace the former temporary facility and serve the increasingly popular resort facilities in the historic 100-Mile House region. The company also announced plans to expand the North Vancouver passenger depot and to replace the existing station at Lillooet, B.C., which was built in 1932. Work on both projects started early in 1986 and the new facilities are scheduled for completion in April of this year.

Following representations from BC Rail in 1984, Transport Canada announced in mid-year that export grain from British Columbia's Peace River region could be shipped to North Vancouver by BC Rail, under the same terms and conditions pertaining to the shipment of prairie grain on Canada's two transcontinental railways.

The federal government also agreed to reimburse BC Rail for the difference between the producer's share and the full compensatory rate to ship grain. The agreement will eliminate BC Rail losses on the handling of export grain and encourage the railway to develop such traffic. Discussions continued during the year regarding a federal government capital contribution for upgrading approximately 60 miles (100 km) of track in the railway's Dawson Creek subdivision. Some of the capital improvements on the Dawson line were carried out in 1985. The balance will be completed in 1986.

In August, a favourable decision from the Canadian Radio-Television and Telecommunications Commission cleared the way for BC Rail's Communications and Data

A new diesel locomotive inspection and repair facility, Prince George.

Processing department to provide private voice and data transmission in competition with the established telephone company. Accordingly, BC Rail may now interconnect with the utility's local distribution lines. The company had merged the former Communications and Data Processing departments some weeks earlier in preparation for the company's entry into the interconnect field.

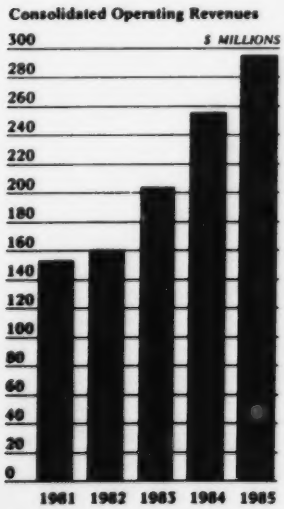
On September 12th, the company's new, $8 million diesel locomotive repair facility was officially opened by Hon. Jack Heinrich, Minister of Education, who joined the company's Board of Directors earlier in the year to replace Hon. Don M. Phillips. The new shop serves the railway's northern fleet of locomotives and will eliminate the need to send northern-based locomotives to Squamish for overhaul work. This will result in considerable cost savings for the company.

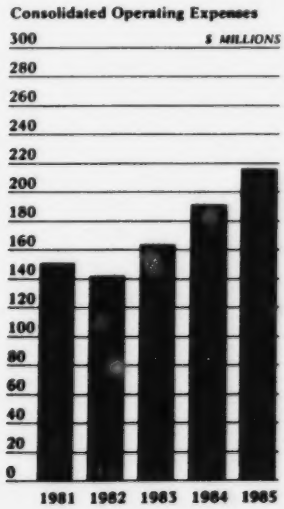
Attempts by the company and its seven-member Council of Trade Unions to reach agreement continued beyond year-end and early in 1986, an agreement covering unionized employees through June, 1987 was reached and ratified. The provincial government earlier had rescinded the British Columbia Railway Dispute Settlement Act, legislation which empowered the government to impose a settlement.

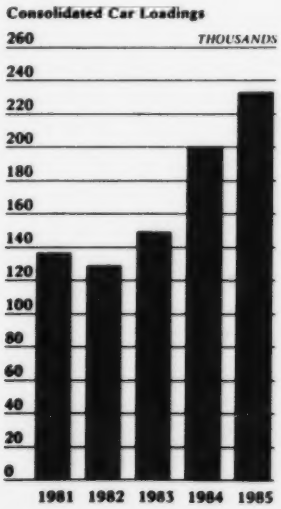
An arbitration board established in 1984 to adjudicate the reduced train crew issue ruled in mid-1985 that the railway could introduce reduced train crews under certain operating conditions. Since that time, a number of yard and road trains have operated with three crew members, rather than four.

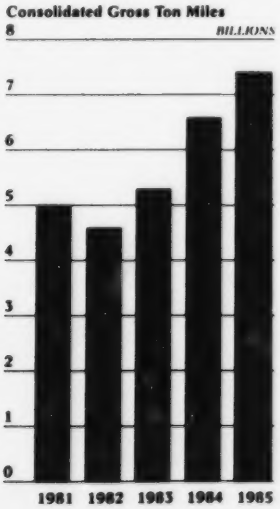
BC Rail's proposed capital expenditure for 1986 has been set at $85.7 million, which ranks as one of the largest corporate capital programs in the province. Of the total, the railway will this year invest a further $33 million in the continuing upgrading of the Prince George to Tacheeda section of the mainline, to accommodate the increasing volume of heavy coal trains and other freight.

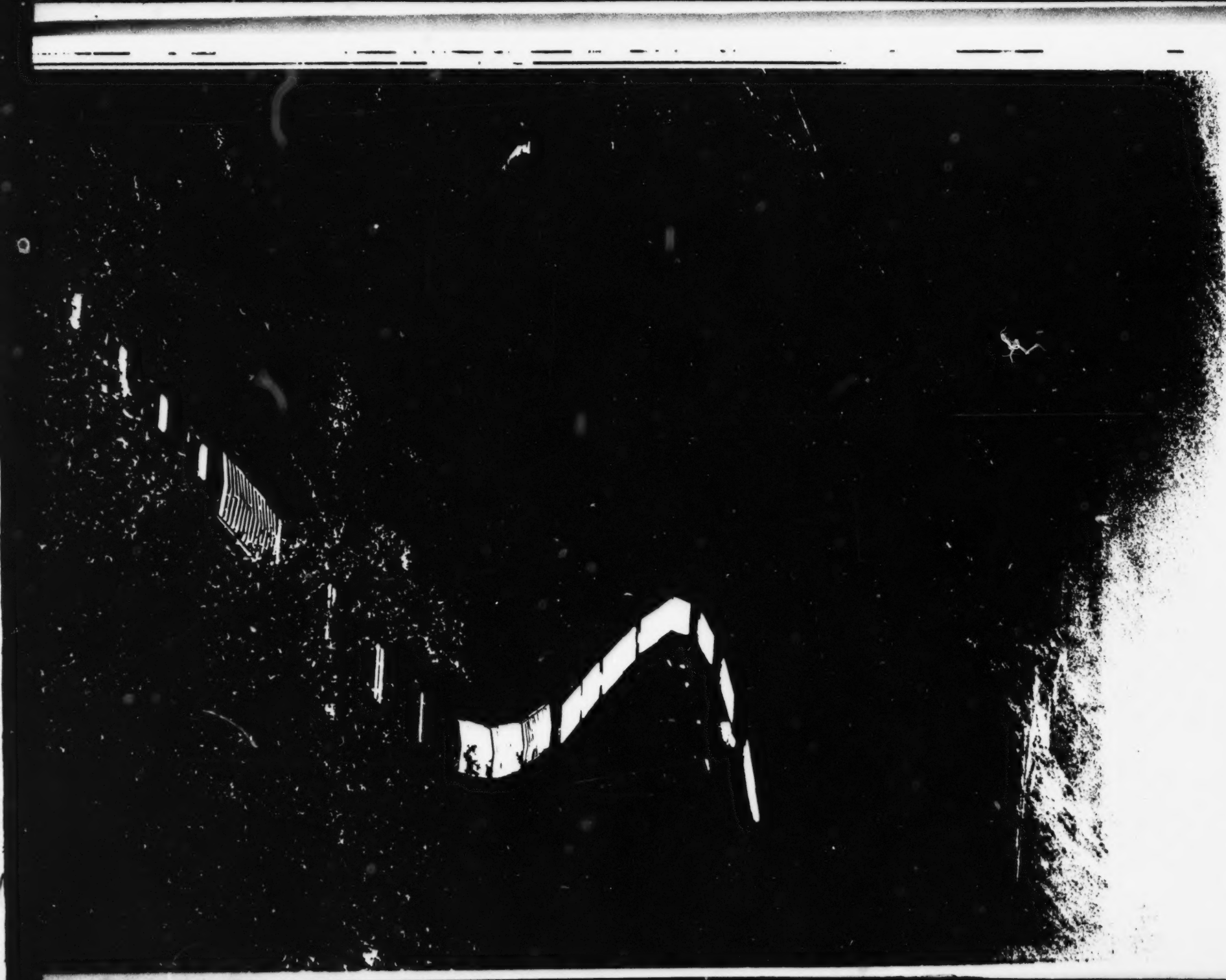
The railway's five-year plan calls for total capital expenditures of more than $388 million, between 1986 and 1990, an average of $77.6 million annually.











BRITISH COLUMBIA RAILWAY COMPANY

CONSOLIDATED FINANCIAL STATEMENTS

Left: High above the Fraser River north of Lillooet, northbound intermodal trailers, with empty bulkhead flats and boxcars make the long, slow haul to the 3,600-foot summit.

BRITISH COLUMBIA RAILWAY COMPANY
MANAGEMENT REPORT

The consolidated financial statements of British Columbia Railway Company have been prepared by management in accordance with generally accepted accounting principles in a manner consistent with the previous year. Management is responsible for the accuracy, integrity and objectivity of the information contained in the financial statements and to ensure that the presentation conforms with generally accepted accounting principles.

The independent auditors, Peat, Marwick, Mitchell & Co., have been appointed by the Lieutenant Governor in Council to express an opinion as to whether these consolidated financial statements present fairly the company's financial position and operating results in conformity with generally accepted accounting principles consistently applied. Their report outlines the scope of their examination and gives their opinion on the fairness of the statement presentation.

The Audit Committee of the railway directors appointed by the Board meets periodically with financial officers of the railway and the external auditors to ensure that each group is fulfilling its obligations and to review and approve the annual financial statements prior to their release.

Management maintains an extensive system of internal accounting controls and believes that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial statements. The adequacy and operation of the control systems are monitored on an on-going basis by an internal audit department.

The Canadian Institute of Chartered Accountants recommends that supplementary information on the effects of changing prices be presented together with the annual financial statements of large publicly-held enterprises. Management does not believe that the development of this information is practicable.

The consolidated financial statements have, in the opinion of the management of the company, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized in Note 1 of the Notes to financial statements.

AUDITORS' REPORT

To the Lieutenant Governor
in Council
Province of British Columbia

We have examined the consolidated balance sheet of British Columbia Railway Company as at December 31, 1985 and the consolidated statements of income and retained earnings, contributed surplus and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1985 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Peat, Marwick, Mitchell & Co.
Chartered Accountants

Vancouver, British Columbia
Canada
March 4, 1986

BRITISH COLUMBIA RAILWAY COMPANY
CONSOLIDATED BALANCE SHEET

	(Dollars in Thousands) December 31	
	1985	1984
Assets		
Current assets		
Cash	$ 10,454	$ 9,649
Accounts receivable	53,539	39,604
Materials and other items	35,181	31,802
	99,174	81,055
Deferred income taxes	1,621	1,954
Property and equipment		
Road and buildings	1,043,446	1,036,583
Equipment	248,858	229,476
	1,292,304	1,266,059
Accumulated depreciation	219,996	195,668
	1,072,308	1,070,391
Dease Lake extension — Note 2	98,020	98,020
	$1,271,123	$1,251,420
Liabilities and Shareholder's Equity		
Current liabilities		
Accounts payable	$ 109,585	$ 85,741
Current obligations on long-term debt	1,329	993
	110,914	86,734
Long-term debt — Note 3	148,875	196,282
Minority interest — Note 4	200,000	200,000
Shareholder's equity		
Share capital — Note 5	257,688	257,688
Contributed surplus	510,716	510,716
Retained earnings	42,930	—
	811,334	768,404
Commitments — Note 6		
Contingent liabilities — Note 7		
	$1,271,123	$1,251,420

On behalf of the Board

S.M. Horner, *Director*

M.C. Norris, *Director*

BRITISH COLUMBIA RAILWAY COMPANY
CONSOLIDATED INCOME AND RETAINED EARNINGS

	(Dollars in Thousands) For the year ended December 31	
	1985	1984
Revenues	$ 294,600	$ 256,108
Expenses		
Operations	67,424	57,028
Equipment	63,102	58,099
Road	38,468	33,693
Depreciation	30,425	26,520
Other	23,438	19,076
Government assistance — Note 8	(6,618)	(5,217)
	216,239	189,199
Railway operating income	78,361	66,909
Non-operating income (expense)		
Interest — Note 9	(18,442)	(46,990)
Debt servicing assistance	—	22,475
	(18,442)	(24,515)
Other income	1,844	1,636
	(16,598)	(22,879)
Net income before deferred income taxes	61,763	44,030
Provision for deferred income taxes — Note 10	333	1,343
Net income before minority interest	61,430	42,687
Minority interest	18,500	8,345
Net income	42,930	34,342
Deficit, beginning of year	—	274,139
Share issue costs less deferred income taxes of $3,297	—	3,044
	42,930	242,841
Transfer to contributed surplus	—	242,841
Retained earnings, end of year	$ 42,930	$ —

BRITISH COLUMBIA RAILWAY COMPANY
CONSOLIDATED CHANGES IN FINANCIAL POSITION

	(Dollars in Thousands) For the year ended December 31	
	1985	1984
Operating activities		
Net income	$ 42,930	$ 34,342
Add (deduct)		
Items not affecting working capital		
Depreciation and amortization	30,425	26,520
Deferred income taxes	333	1,343
Net changes in non-cash working capital		
Accounts receivable	(13,935)	(8,871)
Materials and other items	(3,378)	(1,202)
Accounts payable	26,307	(21,876)
Interest	18,442	24,515
Cash provided by operations	101,124	54,771
Investing activities		
Additions to property and equipment	(33,091)	(66,234)
Changes in payables for equipment purchases	(2,464)	(258)
Government assistance for capital items	749	1,675
	(34,806)	(64,817)
Financing activities		
Issue of long-term debt	192,123	8,013
Repayment of long-term debt	(239,194)	(796,117)
Interest	(18,442)	(24,515)
Government contributions to surplus		
Purchase of sinking funds	—	429,989
Debt servicing	—	6,883
Share issue	—	200,000
Gain on defeasance of debt	—	179,200
Share issue costs	—	(6,341)
	(65,513)	(2,888)
Increase (decrease) in cash	805	(12,934)
Cash, beginning of year	9,649	22,583
Cash, end of year	$ 10,454	$ 9,649

BRITISH COLUMBIA RAILWAY COMPANY
CONSOLIDATED CONTRIBUTED SURPLUS

	(Dollars in Thousands) For the year ended December 31	
	1985	1984
Balance, beginning of year	$ 510,716	$ 137,485
Debt servicing assistance	–	6,883
Refinancing grant	–	429,989
Gain on defeasance of debt	–	179,200
Transferred from deficit	–	(242,841)
Balance, end of year	$ 510,716	$ 510,716

BRITISH COLUMBIA RAILWAY COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 1985

1. Significant Accounting Policies

The accounting regulations prescribed by the Canadian Transport Commission for Canadian railways have been adopted to the extent that this is possible without submitting specific accounting policies and depreciation rates to the Commission for approval.

Basis of consolidation

The consolidated financial statements include the accounts of British Columbia Railway Company and its subsidiaries BC Rail Ltd. and BCR Properties Ltd. In these notes "company" refers to British Columbia Railway Company and its subsidiaries. All significant inter-company transactions are eliminated.

Class of business

The company provides a fully integrated rail freight service within British Columbia. Services other than hauling freight are not of sufficient size to warrant separate reporting.

Road property

New construction is recorded at cost net of Government grants received. Abandoned or relocated sections are removed at average unit costs. Elements of track structure installed during planned programs are recorded at cost and the material replaced is removed at amounts which approximate average unit costs. Labour costs for programmed replacements are expensed as incurred.

All costs of constructing rail lines are capitalized to the date the line is certified operational by the British Columbia Ministry of Transportation and Highways. Capitalization of interest ceases and provision of depreciation commences on the date of certification.

Depreciation

Depreciation is provided for major categories of property and equipment on the straight-line basis at composite rates estimated to reduce the original cost to estimated salvage value over the average service lives of the classes. The group method is used for recording depreciation under which, on disposal, the original cost of assets retired less salvage value is charged against accumulated depreciation. No gain or loss on retirements, other than on accidental destruction of rolling stock and on disposal of land, is included in income. The original cost of assets less estimated salvage value is depreciated over the following number of years.

	Number of years
Grades, surfacing and tunnels	100
Rails	35
Ties	15
Ballast	25
Bridges	30-80
Locomotives and power units	25
Freight cars	33

Based on recent engineering studies, the service life of rail was reduced from 50 to 35 years and ties from 20 to 15 years effective January 1, 1985. This change resulted in an increase in the 1985 depreciation expense of $1,561,000.

Repairs

Repairs and non-programmed replacements of track structure are charged against current operations. Betterments and major track relocations are capitalized.

Materials and supplies

Inventories of materials and supplies are valued at the lower of average cost and net realizable value.

Government assistance

Grants directly related to the construction or rehabilitation of road property have offset related road property capital expenditures. Operating assistance has been deducted from the related expense accounts or included in revenue. Assistance provided by the Province of British Columbia ("Province") during 1984 in its capacity as shareholder has been credited to contributed surplus.

Income taxes

Income tax expense is computed on the basis of accounting income recorded by BC Rail Ltd. No taxes are currently payable as BC Rail Ltd. intends to claim certain amounts for income tax purposes in excess of those recorded in the accounts. British Columbia Railway Company and BCR Properties Ltd. are exempt from Canadian federal and provincial income taxes.

Transactions in foreign currency

Transactions originating in United States currency are translated at the approximate exchange rates prevailing at the dates of the transactions. Assets and liabilities denominated in foreign currency at the balance sheet date are translated to equivalent Canadian amounts at the current rate of exchange.

NOTES

Leases

Certain long-term lease transactions relating to the financing of equipment are accounted for as purchases. The capital lease obligations reflect the present value of future minimum rental payments discounted at the interest rate implicit in the leases. The capitalized values of depreciable assets are generally depreciated over the related lease terms in equal annual amounts. Costs of all other leases are charged against operations as incurred.

2. Dease Lake Extension

These costs consist of charges relating to the uncompleted Dease Lake extension. Construction was suspended in 1977 and there are no commitments to continue. In the event any portion of this extension is abandoned, the cost less any value recovered will be written off at that time.

3. Long-Term Debt

Long-term debt outstanding, less current maturities, consists of the following:

	1985	1984
Sinking fund bonds and debentures payable to the Province		
11% due June 1995	$ 25,000,000	$ —
10.99% due August 2005	24,490,000	—
Bond payable to the Province		
10.75% due February 1990	25,000,000	—
Capital lease obligations — Notes 6 and 12	43,327,000	44,320,000
	117,817,000	44,320,000
Deduct current portion	1,329,000	993,000
	116,488,000	43,327,000
Notes payable to the Province	32,387,000	152,955,000
	$148,875,000	$196,282,000

The notes payable to the Province are arranged under a borrowing agreement between British Columbia Railway Company and the Province. The present notes outstanding bear interest at rates between 8.62% and 11.73%.

4. Minority Interest

The minority interest consists of 8,000,000 series 1-A first preferred shares with a par value of $25 each issued by BC Rail Ltd. These shares are designated as $2.3125 cumulative, redeemable and retractable.

BC Rail Ltd. must make all reasonable efforts in each quarter beginning January 1, 1986 to purchase for cancellation in the open market three-quarters of 1% of the series 1-A preferred shares outstanding at the beginning of the quarter at a price not to exceed $25 per share and all transaction costs. If it is unable to fulfill its obligation in any calendar quarter the obligation will carry over only to the successive calendar quarters of the same calendar year and will thereafter be extinguished.

5. Share Capital

Authorized

10,000,000 shares with a par value of $100 each.

Issued

2,576,885 shares are outstanding and held by the Province.

As all of the shares are held by the Province earnings per share has not been provided.

NOTES

6. Commitments

The company has significant lease commitments for rolling stock and additional minor lease commitments for equipment and real estate which expire at various dates prior to the year 2000. Certain of these leases transfer substantially all of the benefits and risks of ownership to the company and are accounted for as capital assets.

The following is a schedule of future minimum rental payments at December 31, 1985 required under non-cancellable leases that have terms in excess of one year:

	Capital leases	Operating leases
1986	$ 6,569,000	$ 15,499,000
1987	6,569,000	14,945,000
1988	6,569,000	14,617,000
1989	6,569,000	13,577,000
1990	6,569,000	12,219,000
Later years	61,816,000	41,553,000
Total minimum lease payments	94,661,000	$112,410,000
Less		
Executory costs	3,629,000	
Imputed interest	47,705,000	
Present value	$43,327,000	

Assets under capital leases recorded in the property and equipment accounts as at December 31, 1985 are as follows:

Equipment	$46,514,000
Accumulated depreciation	8,773,000
	$37,741,000

As at December 31, 1985 the company had outstanding purchase commitments for the acquisition of property and equipment amounting to $21,000,000.

7. Contingent Liabilities

The company is contingently liable with respect to pending litigation and claims which arose in connection with construction of the Tumbler Ridge rail line and in the normal course of business. In the opinion of management any liability that may arise will be capitalized or would not have a material adverse effect on future income.

8. Government Assistance

Government assistance was as follows:

	1985	1984
Carried forward from previous year	$ 1,031,000	$ —
Received during the year		
From the Province		
Debt related		
Defeasance	—	429,989,000
Servicing	—	29,358,000
Fort Nelson extension		
Operating	3,456,000	3,648,000
Rehabilitation	49,000	145,000
Passenger operation	2,100,000	2,100,000
Passenger car modernization	170,000	500,000
Other	800,000	—
	6,575,000	465,740,000
From the Government of Canada		
Western Grain Transportation Act	879,000	—
Rail line electrification	—	1,675,000
	7,454,000	467,415,000
	8,485,000	467,415,000
Applied as follows		
Operating expenses		
Fort Nelson extension	4,098,000	2,867,000
Passenger operation	2,100,000	2,100,000
Passenger car modernization	420,000	250,000
	6,618,000	5,217,000
Interest expense	—	22,475,000
Revenue	879,000	—
Property and equipment	749,000	1,820,000
Contributed surplus	—	436,872,000
	8,246,000	466,384,000
Carried forward to following year	$ 239,000	$ 1,031,000

NOTES

9. Interest Expense

Interest expense was as follows:

	1985	1984
Interest on long-term debt and notes		
Province	**$14,323,000**	$ 3,663,000
Other	**—**	53,848,000
	14,323,000	57,511,000
Less		
Sinking fund earnings	**—**	5,965,000
Interest capitalized	**—**	6,859,000
Interest earned on temporary investments	**1,150,000**	2,680,000
	1,150,000	15,504,000
	13,173,000	42,007,000
Interest on capital lease obligations	**5,269,000**	4,983,000
	18,442,000	46,990,000
Less		
Application of debt servicing assistance	**—**	22,475,000
Net interest	**$18,442,000**	$24,515,000

10. Income Taxes

The effective tax rate differs from the rate of 52.9% applicable to British Columbia companies because the net income of British Columbia Railway Company and BCR Properties Ltd. is exempt from federal and provincial income taxes. The net income before taxes of BC Rail Ltd., which was $629,000 (1984 — $2,585,000), is subject to federal and provincial income taxes.

11. Pension Plan

The majority of the company's employees participate in a contributory pension plan and are entitled to limited vested rights prior to retirement. An actuarial valuation as at May 31, 1984 disclosed that the plan was fully funded.

12. Related Party Transactions

Related party information not included elsewhere in the notes to financial statements is presented below.

First preferred shares of BC Rail Ltd. and certain capital lease obligations are guaranteed by the Province. The Ministry of Finance of the Province acts as fiscal agent in the administration of the debt and the Superannuation Commission of the Province administers the company pension plan. Fees are charged for both of these services.

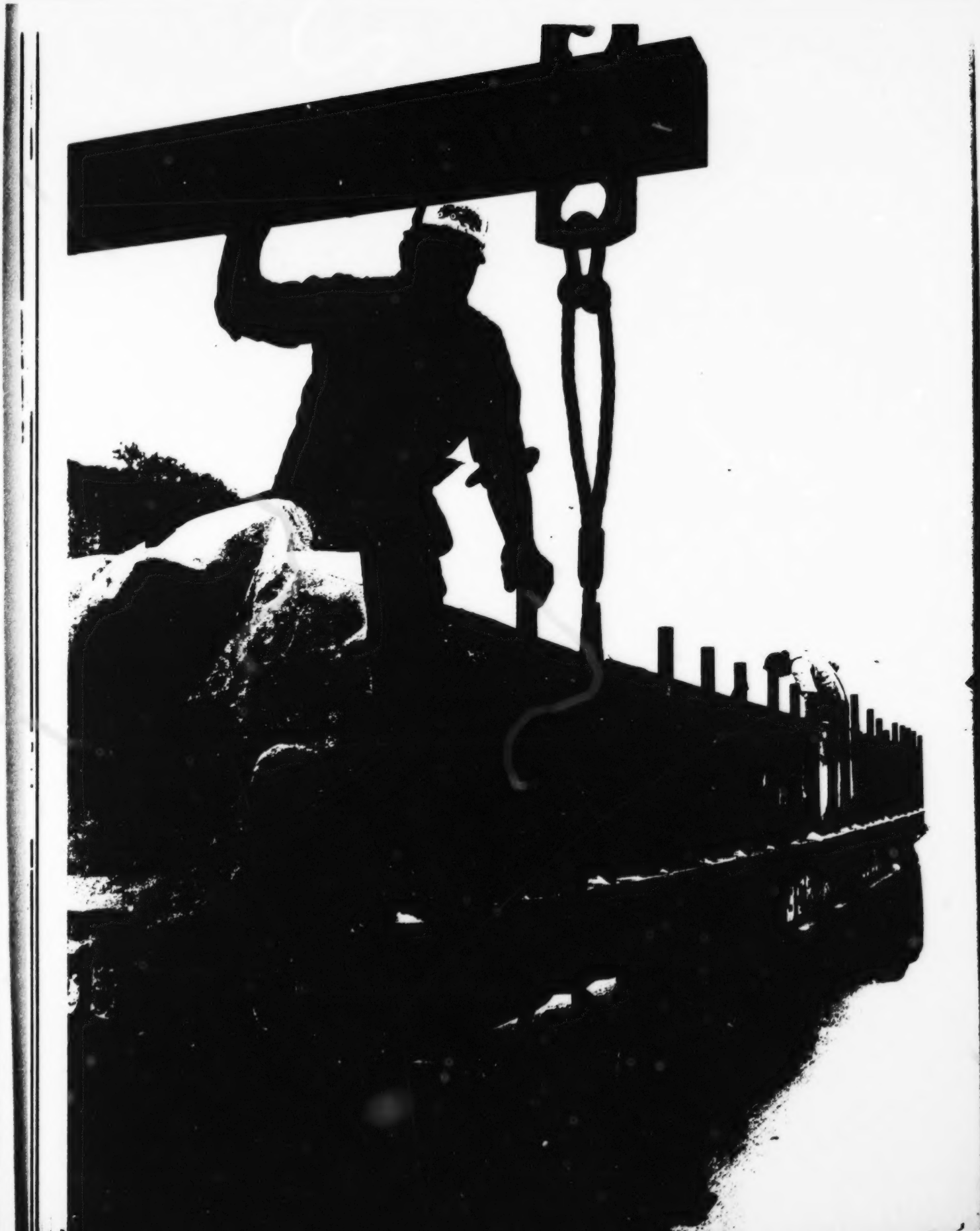
Except as described in Note 10, effective April 1, 1985 the company became subject to all taxes levied by the Province other than property and capital taxes. All other transactions between the company and the Province are at terms no more or less favourable than those with unrelated parties.

13. Reclassification

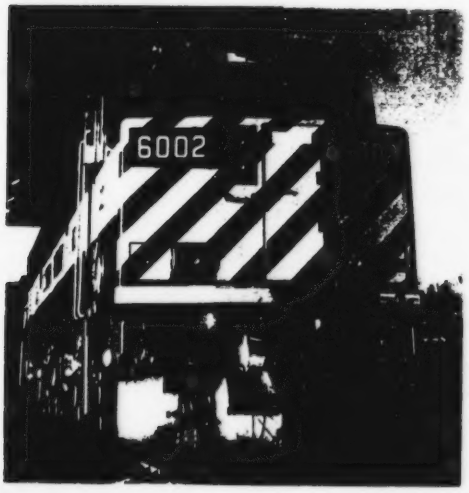
The 1984 information in the statement of changes in financial position has been reclassified to conform with the revised statement format used in 1985.

FIVE YEAR REVIEW

	(Dollars in Thousands) FISCAL YEAR				
CONSOLIDATED STATEMENT	1985	1984	1983	1982	1981
Revenues	$294,600	$256,108	$205,446	$159,696	$152,539
Expenses					
Operations	67,424	57,028	52,432	46,883	47,266
Equipment	63,102	58,099	56,468	45,281	46,146
Road	38,468	33,693	29,372	25,759	28,582
Depreciation	30,425	26,520	18,312	17,436	17,125
Other	23,438	19,076	16,682	15,183	14,176
Government assistance	(6,618)	(5,217)	(7,772)	(8,725)	(3,812)
	216,239	189,199	165,494	141,817	149,483
Railway operating income	78,361	66,909	39,952	17,879	3,056
Non-operating income (expense)					
Interest	(18,442)	(46,990)	(48,633)	(52,303)	(54,800)
Debt servicing assistance	—	22,475	46,367	49,985	52,591
	(18,442)	(24,515)	(2,266)	(2,318)	(2,209)
Other income	1,844	1,636	2,281	3,023	2,318
	(16,598)	(22,879)	15	705	109
Net income before deferred income taxes	61,763	44,030	39,967	18,584	3,165
Provision for deferred income taxes	333	1,343	—	—	—
Net income before minority interest	61,430	42,687	39,967	18,584	3,165
Minority interest	18,500	8,345	—	—	—
Net income	$ 42,930	$ 34,342	$ 39,967	$ 18,584	$ 3,165
OPERATING STATISTICS					
Total revenue cars loaded on line	232,115	197,643	145,571	126,031	131,624
Received from connections	2,220	2,614	3,198	2,546	3,358
Total carloadings	234,335	200,257	148,769	128,577	134,982
MOTIVE POWER					
Electric locomotives	7	7	7	—	—
Diesel locomotives	110	115	123	126	126
ROLLING STOCK FLEET					
Freight cars	9,960	10,060	9,690	9,811	9,855
Passenger cars	9	9	9	6	6
Boarding and work cars	452	469	446	493	504
TONS HAULED	17,831,967	14,672,412	9,347,197	8,023,581	8,323,124
EMPLOYEES AT YEAR END	2,620	2,640	2,600	2,400	2,500



BC RAIL LTD.



FINANCIAL STATEMENTS

Left: Salt for highway use unloading in Prince George

BC RAIL LTD.
MANAGEMENT REPORT

The financial statements of BC Rail Ltd. have been prepared by management in accordance with generally accepted accounting principles in a manner consistent with the previous year. Management is responsible for the accuracy, integrity and objectivity of the information contained in the financial statements and to ensure that the presentation conforms with generally accepted accounting principles.

The independent auditors, Peat, Marwick, Mitchell & Co., have been appointed by the Shareholders to express an opinion as to whether these financial statements present fairly the company's financial position and operating results in conformity with generally accepted accounting principles consistently applied. Their report outlines the scope of their examination and gives their opinion on the fairness of the statement presentation.

The Audit Committee of the railway directors appointed by the Board meets periodically with financial officers of the railway and the external auditors to ensure that each group is fulfilling its obligations and to review and approve the annual financial statements prior to their release.

Management maintains an extensive system of internal accounting controls and believes that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial statements. The adequacy and operation of the control systems are monitored on a[n] on-going basis by an internal audit department.

The Canadian Institute of Chartered Accountants recommend[s] that supplementary information on the effects of changing prices be presented together with the annual financial statements of large publicly-held enterprises. Management does not believe that the development of this information is practicable.

The financial statements have, in the opinion of the management of the company, been properly prepare[d] within reasonable limits of materiality and within the framewo[rk] of the accounting policies summarized in Note 1 of the Notes to financial statements.

AUDITORS' REPORT

To the Shareholders

We have examined the balance sheet of BC Rail Ltd. as at December 31, 1985 and the statements of income and deficit, contributed surplus and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the company as at December 31, 1985 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Peat, Marwick, Mitchell

Peat, Marwick, Mitchell & Co.
Chartered Accountants

Vancouver, British Columbia
Canada
March 4, 1986

BC RAIL LTD.
BALANCE SHEET

	(Dollars in Thousands) December 31	
	1985	1984
Assets		
Current assets		
Cash	$ 10,452	$ 9,643
Accounts receivable	53,539	39,604
Materials and other items	34,545	31,778
Due from British Columbia Railway Company	36,903	10,885
	135,439	91,910
Deferred income taxes	1,621	1,954
Property and equipment		
Road and buildings	1,040,200	1,033,327
Equipment	248,858	229,476
	1,289,058	1,262,803
Accumulated depreciation	219,996	195,668
	1,069,062	1,067,135
Dease Lake extension — Note 3	98,020	98,020
	$1,304,142	$1,259,019
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable	$ 107,364	$ 85,740
Current obligations on long-term debt	1,137	993
Due to BCR Properties Ltd.	31,565	29,961
	140,066	116,694
Long-term debt — Note 4	640,737	598,782
Shareholders' equity		
Share capital — Note 5	411,690	411,690
Contributed surplus	113,155	133,655
Deficit	(1,506)	(1,802)
	523,339	543,543
Commitments — Note 6		
Contingent liabilities — Note 7		
	$1,304,142	$1,259,019

On behalf of the Board

S.M. Horner, *Director*

M.C. Norris, *Director*

BC RAIL LTD.
INCOME AND DEFICIT

	(Dollars in Thousands) For the year ended December 31	
	1985	1984 *(Note 2)*
Revenues	$ 294,600	$ 149,732
Expenses		
Operations	67,424	31,685
Equipment	63,102	31,619
Road	38,468	19,098
Depreciation	30,425	14,923
Other	23,378	10,751
Government assistance — Note 8	(6,618)	(2,153)
	216,179	105,923
Railway operating income	78,421	43,809
Non-operating income (expense)		
Interest — Note 9	(78,065)	(41,479)
Other income	273	255
Net income before deferred income taxes	629	2,585
Provision for deferred income taxes	333	1,343
Net income	296	1,242
Deficit, beginning of year	1,802	—
Share issue costs less deferred income taxes of $3,297	—	3,044
Deficit, end of year	$ 1,506	$ 1,802

BC RAIL LTD.
CONTRIBUTED SURPLUS

	(Dollars in Thousands) For the year ended December 31	
	1985	1984 *(Note 2)*
Balance, beginning of year	$ 133,655	$ —
Allocated on the issue of common shares	—	150,000
	133,655	150,000
Dividends paid		
Preferred shares	18,500	8,345
Common shares	2,000	8,000
	20,500	16,345
Balance, end of year	$ 113,155	$ 133,655

BC RAIL LTD.
CHANGES IN FINANCIAL POSITION

	(Dollars in Thousands) For the year ended December 31	
	1985	1984 *(Note 2)*
Operating activities		
Net income	$ 296	$ 1,242
Add (deduct)		
Items not affecting working capital		
Depreciation and amortization	30,425	14,923
Deferred income taxes	333	1,343
Net changes in non-cash working capital		
Accounts receivable	(13,935)	(39,604)
Materials and other items	(2,767)	(31,778)
Accounts payable	24,088	80,563
Intercompany accounts	(24,414)	19,076
Interest	78,065	41,479
Cash provided by operations	92,091	87,244
Investing activities		
Additions to property and equipment	(33,101)	(1,180,153)
Change in payables for equipment purchases	(2,464)	5,177
Government assistance for capital items	749	75
	(34,816)	(1,174,901)
Financing activities		
Issue of long-term debt	196,047	746,944
Repayment of long-term debt	(153,948)	(147,169)
Interest	(78,065)	(41,479)
Share issue	–	411,690
Share issue costs	–	(6,341)
Contributed capital	–	150,000
	(35,966)	1,113,645
Dividends paid	(20,500)	(16,345)
Increase in cash	809	9,643
Cash, beginning of year	9,643	–
Cash, end of year	$ 10,452	$ 9,643

BC RAIL LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 1985

1. Significant Accounting Policies

The accounting regulations prescribed by the Canadian Transport Commission for Canadian railways have been adopted to the extent that this is possible without submitting specific accounting policies and depreciation rates to the Commission for approval.

Class of business

The company provides a fully integrated rail freight service within British Columbia. Services other than hauling freight are not of sufficient size to warrant separate reporting.

Road property

New construction is recorded at cost net of Government grants received. Abandoned or relocated sections are removed at average unit costs. Elements of track structure installed during planned programs are recorded at cost and the material replaced is removed at amounts which approximate average unit costs. Labour costs for programmed replacements are expensed as incurred.

All costs of constructing rail lines are capitalized to the date the line is certified operational by the British Columbia Ministry of Transportation and Highways. Capitalization of interest ceases and provision of depreciation commences on the date of certification.

Depreciation

Depreciation is provided for major categories of property and equipment on the straight-line basis at composite rates estimated to reduce the original cost to estimated salvage value over the average service lives of the classes. The group method is used for recording depreciation under which, on disposal, the original cost of assets retired less salvage value is charged against accumulated depreciation. No gain or loss on retirements, other than on accidental destruction of rolling stock and on disposal of land, is included in income. The original cost of assets less estimated salvage value is depreciated over the following number of years.

	Number of years
Grades, surfacing and tunnels	100
Rails	35
Ties	15
Ballast	25
Bridges	30-80
Locomotives and power units	25
Freight cars	33

Based on recent engineering studies, the service life of rail was reduced from 50 to 35 years and ties from 20 to 15 years effective January 1, 1985. This change resulted in an increase in the 1985 depreciation expense of $1,561,000.

Repairs

Repairs and non-programmed replacements of track structure are charged against current operations. Betterments and major track relocations are capitalized.

Materials and supplies

Inventories of materials and supplies are valued at the lower of average cost and net realizable value.

Government assistance

Grants directly related to the construction or rehabilitation of road property have offset related road property capital expenditures. Operating assistance has been deducted from the related expense accounts or included in revenue.

Income taxes

Income tax expense is computed on the basis of accounting income recorded by the company. No taxes are currently payable as the company intends to claim certain amounts for income tax purposes in excess of those recorded in the accounts.

Transactions in foreign currency

Transactions originating in United States currency are translated at the approximate exchange rates prevailing at the dates of the transactions. Assets and liabilities denominated in foreign currency at the balance sheet date are translated to equivalent Canadian amounts at the current rate of exchange.

Leases

Certain long-term lease transactions relating to the financing of equipment are accounted for as purchases. The capital lease obligations reflect the present value of future minimum rental payments discounted at the interest rate implicit in the leases. The capitalized values of depreciable assets are generally depreciated over the related lease terms in equal annual amounts. Costs of all other leases are charged against operations as incurred.

NOTES

2. Prior Year Information

The company commenced railway operations on June 19, 1984 with the purchase from British Columbia Railway Company of all of that company's railway assets and undertaking, except industrial parks and certain undeveloped lands.

The company's operations prior to June 19, 1984 were discontinued. As they were not material in relation to the railway operations comparative information is for the period commencing June 19, 1984.

3. Dease Lake Extension

Included in the assets acquired from British Columbia Railway Company were costs related to the uncompleted Dease Lake extension. Construction was suspended in 1977 and there are no commitments to continue. In the event any portion of this extension is abandoned, the cost less any value recovered will be written off at that time.

4. Long-Term Debt

Long-term debt outstanding, less current maturities, consists of the following:

	1985	1984
Capital lease obligations — Notes 6 and 11	$ 43,327,000	$ 44,320,000
Deduct current portion	1,137,000	993,000
	42,190,000	43,327,000
Notes payable to British Columbia Railway Company		
10.75% due February 1990	25,000,000	—
10.4% due June 1995	56,350,000	—
12.75% due July 1995	114,697,000	—
	196,047,000	—
Notes payable to BCR Properties Ltd. 14% due June 1999	402,500,000	402,500,000
Notes payable to the Province of British Columbia ("Province")	—	152,955,000
	$640,737,000	$598,782,000

5. Share Capital

Authorized

5,000,000 common shares with a par value of $100 each.

20,000,000 first preferred shares with a par value of $25 each of which 8,000,000 are designated as $2.3125 cumulative redeemable retractable first preferred shares, series A.

20,000,000 second preferred shares with a par value of $100 each of which 3,000,000 have been designated as non-cumulative redeemable second preferred shares, series A.

Issued and outstanding	
500,012 common shares	$ 50,001,000
8,000,000 series 1-A preferred shares (Note 6)	200,000,000
1,616,892 series 2-A preferred shares	161,689,000
	$411,690,000

Earnings per common share are not provided as all of the shares are held by British Columbia Railway Company and its wholly owned subsidiary.

6. Commitments

The company has significant lease commitments for rolling stock and additional minor lease commitments for equipment and real estate which expire at various dates prior to the year 2000. Certain of these leases transfer substantially all of the benefits and risks of ownership to the company and are accounted for as capital assets.

The following is a schedule of future minimum rental payments at December 31, 1985 required under non-cancellable leases that have terms in excess of one year:

	Capital leases	Operating leases
1986	$ 6,569,000	$ 15,499,000
1987	6,569,000	14,945,000
1988	6,569,000	14,617,000
1989	6,569,000	13,577,000
1990	6,569,000	12,219,000
Later years	61,816,000	41,553,000
Total minimum lease payments	94,661,000	$112,410,000

Less	
Executory costs	3,629,000
Imputed interest	47,705,000
Present value	$43,327,000

Assets under capital leases recorded in the property and equipment accounts as at December 31, 1985 are as follows:

Equipment	$46,514,000
Accumulated depreciation	8,773,000
	$37,741,000

As at December 31, 1985 the company had outstanding purchase commitments for the acquisition of property and equipment amounting to $21,000,000.

The company must make all reasonable efforts in each quarter beginning January 1, 1986 to purchase for cancellation in the open market three-quarters of 1% of the series 1-A preferred shares outstanding at the beginning of the quarter at a price not to exceed $25 per share and all transaction costs. If it is unable to fulfill its obligation in any calendar quarter the obligation will carry over only to the successive calendar quarters of the same calendar year and will thereafter be extinguished.

7. Contingent Liabilities

The company is contingently liable with respect to pending litigation and claims which arose in connection with construction of the Tumbler Ridge rail line and in the normal course of business. In the opinion of management any liability that may arise will be capitalized or would not have a material adverse effect on future income.

8. Government Assistance

Government assistance was as follows:

	1985	1984
Carried forward from previous year	$ 1,031,000	$ 70,000
Received during the year		
From the Province		
Fort Nelson extension		
Operating	3,456,000	1,641,000
Rehabilitation	49,000	75,000
Passenger operation	2,100,000	1,115,000
Passenger car modernization	170,000	428,000
Other	800,000	—
	6,575,000	3,259,000
From the Government of Canada		
Western Grain Transportation Act	879,000	—
	7,454,000	3,259,000
	8,485,000	3,329,000
Applied as follows		
Operating expenses		
Fort Nelson extension	4,098,000	860,000
Passenger operation	2,100,000	1,115,000
Passenger car modernization	420,000	178,000
	6,618,000	2,153,000
Revenue	879,000	—
Property and equipment	749,000	145,000
	8,246,000	2,298,000
Carried forward to following year	$ 239,000	$1,031,000

9. Interest Expense

Interest expense was as follows:

	1985	1984
Notes payable		
BCR Properties Ltd.	$56,350,000	$31,011,000
British Columbia Railway Company	17,499,000	10,337,000
	73,849,000	41,348,000
Short-term notes payable to the Province	3,071,000	3,663,000
Capital lease obligations	5,269,000	2,752,000
	82,189,000	47,763,000
Less interest income		
Related companies	2,974,000	4,978,000
Other	1,150,000	1,306,000
	4,124,000	6,284,000
	$78,065,000	$41,479,000

10. Pension Plan

The majority of the company's employees participate in a contributory pension plan and are entitled to limited vested rights prior to retirement. An actuarial valuation as at May 31, 1984 disclosed that the plan was fully funded.

NOTES

11. Related Party Transactions

Related party information not presented elsewhere in the notes to financial statements is presented below.

All of the outstanding common and second preferred shares of the company are owned as follows:

BCR Properties Ltd. (a wholly-owned subsidiary of British Columbia Railway Company)	75%
British Columbia Railway Company	25%

First preferred shares and certain capital lease obligations are guaranteed by the Province. The Ministry of Finance of the Province acts as fiscal agent in the administration of the debt and the Superannuation Commission of the Province administers the company pension plan. Fees are charged for both of these services.

The company is subject to provincial income taxes and effective April 1, 1985 became subject to all other taxes levied by the Province except property and capital taxes. All other transactions between the company and its Shareholders are at terms no more or less favourable than those with unrelated parties.

12. Reclassification

The 1984 information in the statement of changes in financial position has been reclassified to conform with the revised statement format used in 1985.

Overleaf: Raw materials awaiting processing for pulp and paper manufacture.

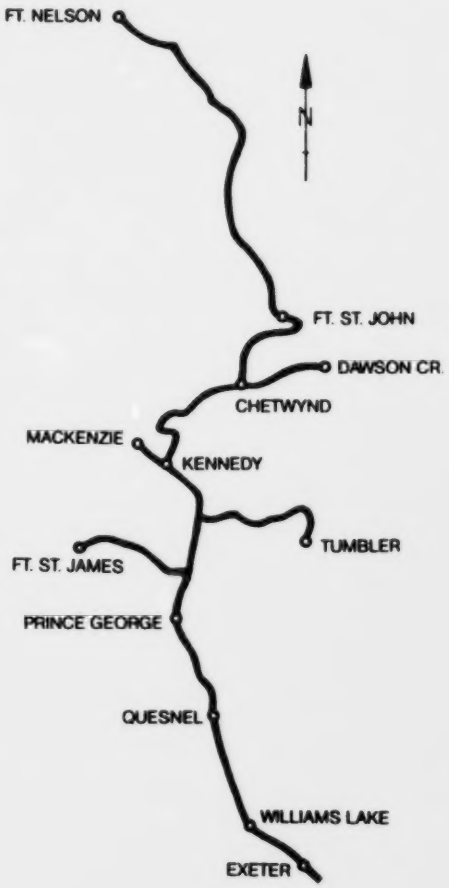
SALUTE TO BC RAIL'S NORTH

"This company was created to carry the natural resources of central and northern British Columbia to markets around the world. With this report, we salute and thank our north and central interior shippers, who over many years, have contributed so much to the success and development of BC Rail."

M.C. Morris

President and Chief Executive Officer

SALUTE TO BC RAIL'S NORTH



In Canada, "The North" means many things to many people.

We live in a vast country stretching from a latitude of 46.5 degrees at Windsor, Ont., in the south, to Ellesmere Island in the Arctic Circle.

To the citizens of Tuktoyaktuk, on the shores of the Beaufort Sea, at 69.3 degrees north, the north may be the tiny outpost of Resolute, on Cornwallis Island, at 74.5 degrees north.

But to the people at BC Rail, the north begins around Williams Lake and continues to Fort Nelson, 660 miles away, at latitude 58.48 degrees north.

Like a great river, the mainline and its tributaries — rail extensions to Tumbler Ridge, Fort St. James, and Dawson Creek — collect the products of our land and people and take them to markets all over the world.

It is rich country — and it is the heart of the railway. About 80 per cent of the traffic carried by BC Rail originates at points north of and including Williams Lake.

Last year, this amounted to 211,660 carloads of freight. Of these, 83,400 carloads were coal shipped from Tumbler Ridge. The remaining 128,260 contained forest products and other commodities.

Excluding coal traffic, nearly 29,000 carloads of freight were shipped from the Peace area, 73,500 from the interior (Quesnel to Mackenzie) and 25,760 from the Cariboo and north of Williams Lake.

The railway also provided passenger service to 77,755 passengers in 1985, an important contribution to local transportation needs and the promotion of tourist traffic in the north central interior, the Cariboo and further south.

Directly and indirectly, many people rely on the railway for their livelihood. Nearly half of BC Rail's work force is based in the north. And along the line, more than 5,000 people work for companies located on property leased from the railway.

Hundreds more are employed in companies which, while not located on BC Rail property, regularly use BC Rail to transport their products.

It is hard to imagine the province without the railway. Equally, it is difficult to imagine the railway without the communities and the people it serves. Its success and existence depend on those who depend on it.

The railway today is the product of a dream of "The North" that began in 1912 when promoters launched the Pacific Great Eastern Railway — a grand name for a glorious vision of vast, untapped wealth in a new land.

It was a dream that collapsed almost immediately, a few years later, when the railway was unable to redeem its bonds and the province was forced to assume ownership.

Over the years that followed, successive provincial governments either ignored or extended the railway, depending on the whims of the politicians involved. And the dream lurched forward, from "Nowhere to Nowhere", as some critics joked.

But the dream of this fabulous north, in many ways more like a nightmare, would not die. Not until 1977, when work on the Dease lake extension was halted and supplanted by a more modest vision of the north — a vision no longer determined by the dreams of politicians but founded on true economic realities.

Latter day politicians discovered that there are limits to all dreams. And out of that was born a new beginning for the railway — an opportunity to prove itself capable of surviving unaided as a legitimate commercial enterprise.

Today's railway serves 12 of northern B.C.'s larger communities, with a combined population of nearly 300,000 people — including many in unorganized areas.

After Canada's two transcontinental railways, BC Rail is the third largest in the country. Its line passes through the Coast Mountain region, the interior plateau and the Rocky Mountains. Today, the reality is even greater than the dream.

In recent years, the railway's most spectacular achievement has been the construction of a new line serving the province's northeastern coal development. Five years ago, the town of Tumbler Ridge, population 5,000, didn't exist. Today, it is home base for BC Rail's electrified, 98-car unit trains, which carry thermal and metallurgical coal to the hungry steelworks of Japan.

The line to the Rocky Mountain coal-fields was completed ahead of schedule in 1983. Since then, 14 million tons of coal have been shipped to Japan.

But the coal story is recent. Throughout the rest of the railway's history, its most important freight has been forest products, which annually accounted for more than 80 per cent of total tonnage. Equally important, but in smaller quantities, were minerals, petrochemicals and other resource commodities. And there are some encouraging signs of renewed economic interest and activity.

A mile-or-more of interior lumber awaits a green light to start the 465-mile haul south to Vancouver.

In the Peace country, near Dawson Creek, production is expected to start soon at a new, $40 million waferboard plant, to be built on the BC Rail line near this community.

About 125 people will be employed in the plant, to be constructed by the U.S.-based firm, Louisiana Pacific, and about eight to 10 carloads of freight a day are initially expected.

In Prince George, about 110 new jobs are to be created by the recently-opened CanAspen Manufacturing Ltd., a company manufacturing chopsticks for export to Japan.

The plant is a welcome contribution to the growth of a new forest products industry, an industry based on badly-needed secondary manufacturing. In addition, the chopsticks will be made from aspen, formerly regarded as a weed species.

Another major development in Prince George is a new, $4-$5 million, 60,000-square foot research and development park by Caledonia Research, with construction expected soon. The project, on 20 acres of land, will employ about 100 people.

In addition, Prince George has consolidated its position as one of the province's major distribution, retail and administrative centres — and certainly, it is the hub of BC Rail's north.

Forest industry plants and mills in the interior and the Cariboo have continued to upgrade during the recession. Computerization and new technology have improved productivity, making the industry one of the most competitive on the continent.

In the Cariboo, Gibraltar Mines Ltd. plans a $17 million leeching plant at its mine 30 miles north of Williams Lake. The new plant, expected to be completed by late fall, will extract more copper from waste tailings at the minesite.

About 200 new jobs are expected to be created when the Blackdome mine in the South Cariboo goes into production in early summer.

The logging industry in the Cariboo has been growing healthier, as lumber markets continue to improve. As well, thousands of square miles of timber, threatened by a mountain pine beetle infestation, have been opened up for new logging. The timber is currently sound, but it must be harvested quickly before it deteriorates.

For 74 years, the railway has been successfully meeting the challenges the north continues to throw out — and this salute to this vital constituency of BC Rail is in recognition of the contribution its people and industries have made to the growth and development of the railway.

The railway's and the north's fortunes are inextricably linked — in what is hoped will continue to be a mutually rewarding interdependence.

Page 33: This tribute to BC Rail's northern communities and shippers was hand-carved from western white spruce, donated by Rustad Bros., Prince George. It was hand-carved by BC Rail employee Noel Van Sandwyk.

Lumber flats awaiting switching in BC Rail's Prince George yard.

CONTACT INFORMATION

Some of the BC Rail people who helped make 1985 a record year.

NOTICE OF SPECIAL MEETING
For Non-voting Preferred Shareholders

In accordance with the practice established last year, the Board of Directors and Management of BC Rail Ltd. cordially invite preferred shareholders to an informational meeting, on June 19th, 1986. The meeting will start at 10:30 a.m., and be held in the Commonwealth East Ballroom of the Holiday Inn Harbourside, 1133 West Hastings St., Vancouver, B.C.

The meeting is not a legal requirement and is offered as a courtesy to the company's preferred shareholders. Its purpose is to report on company activities and performance during 1985 and on the outlook for the coming operational year. The informational meeting is open to the public. It follows the company's Annual General Meeting, which is open only to common shareholders, directors and officers of the company.

For further information, please call:
Mrs. M.H. Hatch,
(604) 986-2012

If you would like more copies of this report or additional information about the British Columbia Railway group of companies, please call or write:

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